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SUBJECT: SOUTH AFRICA INPUT FOR 2009 AGOA ELIGIBILITY REVIEW

REF: SECSTATE 85086

1. In response to Ref A, Post provides the following input for the 2009 AGOA eligibility review.

Country Background Summary

2. The population of South Africa was 48.7 million in mid-2008. In 2007, South African Gross National Income (GNI) was \$255 billion; GNI per capita was \$5,390. South African exports to the U.S. were \$9.1 billion in 2007, an increase of 22% from 2006. Platinum group metals were the biggest export item to the U.S., followed by vehicles and transport equipment. Over 98% of South Africa's exports to the U.S. were duty-free in 2007 due to the combination of AGOA, GSP benefits, and South Africa's most-favored nation status.

Market-based Economy

3. Major Strengths Identified: South Africa continues to make progress in deepening its market-based economy. Government expenditure as a percentage of GDP is lower than the OECD average. That is partially due to the fact that the country does not have a national pension system. The economy has achieved record growth on the strength of the private sector and robust domestic demand. The real annualized economic growth during the four quarters of 2007 was 5.5 percent (revised from 5.1). The forecast for growth is 3.5 to 4.0 in 2008 with a similar level of growth expected in 2009. The government has set sound macroeconomic objectives, and has managed to eliminate the fiscal deficit. The government had a fiscal surplus of 0.3% of GDP in 2007. Inflation (CPIX, or consumer price inflation less mortgage costs) was relatively high at 13% in August 2008. Increasing food and fuel prices have pushed CPIX above the upper end of the 3% to 6% inflation target range for the better part of 2007 and 2008. Strong fundamentals, comparatively high interest rates, and the view that the rand is essentially a commodity-based currency have kept the value of the rand strong. However, in 2007 the rand started to depreciate following turbulence in the global financial markets and concerns about South Africa's large current account deficit. This caused the rand to depreciate from about R7/1USD in early June 2007 to almost R8.2/1USD in September 2008. In June 2008, the South African Reserve Bank (SARB) hiked its policy interest rate for the 10th time since June 2006. The SARB's tightened monetary policy can be attributed to higher food and oil prices, continued growth in domestic credit, and a weaker rand. The SARB now expects inflation to remain above the target range until the second half of 2010.

4. Poverty and unemployment, compounded by the impact of HIV/AIDS on the work force, remain serious issues. Official

unemployment was 23.1% in June 2008 and total unemployment (including discouraged workers who did not actively seek employment, was 35%. Researchers estimate that the country needs 6.0% growth for a decade or more to halve unemployment (i.e., to reach an official unemployment target of 15%). The strong rand has been problematic for labor-intensive industries and exporters of all kinds, especially for textiles and apparel. The depreciation in the rand during the last half of 2007 and 2008 has improved the position of these industries in 2008. The growth in the economy has also led to an unexpectedly large current account deficit. South Africa's current account deficit has grown steadily, reaching 7.3% of GDP in the second quarter of 2008. Such levels expose South Africa to the risk of a sharp currency depreciation should capital inflows fall off dramatically. Looking forward, the current account is likely to improve, albeit modestly, during the remainder of 2008 on the back of an improvement in mining production and a slowdown in the domestic economy, and hence import demand. The economy is still encumbered by new regulations and layers of bureaucratic regulation that can inhibit domestic and foreign investment. Many government departments and agencies suffer severe capacity constraints and have thus been unable to implement programs on time and with minimal confusion. The economy is still hampered by severe skills shortages in all sectors. U.S. firms are supportive of the aims of the government's Black Economic Empowerment (affirmative action) program, but they continue to have reservations about the implementation of regulations and provisions calling for 25% equity ownership for large and medium-sized companies by black, or formerly disadvantaged, groups in South Africa. Infrastructure bottlenecks and shortages, including growing

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electrical power outages, limit growth investment. High crime levels add increased costs to businesses.

Political Reforms/Rule of Law/Anti-Corruption

15. Major Strengths Identified: In April 2004, South Africa held free and fair elections in which the ruling African National Congress (ANC) won nearly 70% of the vote. Seats in the Parliament's National Assembly are allocated based on the percentage of votes each party receives. In the 2004 elections, the ANC won 279 of the 400 seats in the Assembly, followed by the Democratic Alliance, which won 50 seats, and the Inkatha Freedom Party, which took 28. Subsequent "floor-crossing" periods, in which MPs were allowed to change parties, resulted in the ANC gaining 20 more seats for a total of 297. The Cabinet includes 28 ministers from the ANC and one from the Azanian People's Organization (AZAPO). Mbeki extended the cabinet to include ANC Deputy President and current state president Kgalema Molanthe as minister without portfolio. Upon Mbeki's forced resignation in September 2008, the AZAPO minister, along with eleven other cabinet ministers, resigned with Mbeki. The Constitution's bill of rights provides for due process including the right to a fair and public trial within a reasonable time of being charged, and the right to appeal to a higher court. South Africa has an excellent anticorruption regulatory framework, highlighted by the passage of the Prevention and Combating of Corrupt Activities Act of 2004. For the first time, the Act defined the scope of corrupt activities and thus is a welcome complement to other anticorruption laws. Mbeki made the fight against corruption a hallmark of his administration. ANC parliamentarians, and provincial and municipal officials have been charged, arrested, and convicted of corruption, signaling official discouragement of this practice. In addition, the ruling ANC ousted five MPs from the party and Parliament who were found guilty of pocketing Parliamentary travel funds. Mbeki lost the leadership of the ANC to Jacob Zuma in December 2007 at the party's national congress in Polokwane. Mbeki resigned from the position of President of

South Africa on September 25, 2008 after the ANC recalled him from the position of President and he was replaced by President and ANC Deputy President Kgalema Motlanthe. Elections are scheduled for April 2009.

16. Major Issues/Problems Identified: Police use of lethal force against suspects resulted in a significant number of deaths, and deaths in police custody were a problem. The government investigated and punished some abusers. Violent crime is high, frightens the public, discourages investment, and strains the judicial system. Severe prison and prolonged pretrial detention are problems. Despite advances against corruption, there is still the widespread view that corruption is present in some parts of the government, particularly within the South African Police Service and the Department of Home Affairs. In May 2008, xenophobic attacks aimed at African foreigners and some South African ethnic minorities broke out and spread nationwide. Sixty-two people died and about 100,000 people were displaced in connection with the attacks. Other deaths have occurred as the displaced persons returned to their original or other communities.

Poverty Reduction

17. Major Strengths Identified: Mbeki continued to make the reduction in poverty and the raising of the level of employment cornerstones of his second term in office. Years of fiscal discipline by the SAG are making it possible for the government to reduce the interest cost of the national debt, lower marginal tax rates and increase government expenditures on social programs and capital expenditures. As a result, government expenditure on social programs has doubled in the last five years. In February 2008, Finance Minister Trevor Manuel presented this year's budget to Parliament. Once again, the government increased spending on poverty reduction and social services such as access to housing, electricity, sanitation, child and pension grants, education, and HIV/AIDS programs. The government also allocated new funds to prepare for the 2010 World Cup, including budget allocation for new roads and energy infrastructure. In an effort to stimulate faster growth, generate employment and improve the country's competitiveness, government expenditure for infrastructure spending totals some \$50 billion between 2007 and 2010. Of this, about 40% will be spent by public enterprises, mostly

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Eskom (\$11 billion covering energy generation, transmission and distribution) and Transnet (\$6 billion, of which \$5 billion will go towards harbors, ports, railways and petroleum pipelines). In 2004, Mbeki launched the Expanded Public Works Program, a major new jobs initiative similar to U.S. Depression-era work programs. The objective is to create one million temporary jobs, and in so doing impart skills and bring more of the unemployed into the mainstream workforce. Jobs and skills are increasing through the government's Expanded Public Works Programme (EPWP) and small farmers are benefiting from the Agriculture Starter Pack Programme and the Comprehensive Agricultural Support Programme. The cumulative number of total new work opportunities created under the EPWP since its commencement in April 2004 through December 2007 is at least 776,190. It is expected that the program will exceed its target of one million work opportunities, set for its first five years. The government introduced programs to supply free basic water and electricity to all, and has been working to expand its low and no-income housing programs. More than 2.3 million subsidized housing units have been built since 1994. Since 1994, 10 million more people have access to clean water. The government raised the age of eligibility for child support grants to cover all children up to the age of 14. The government increased welfare grants going to old age

pensioners, reducing the qualifying age of men from 65 to 60 years phased over a period of three years. The government also increased welfare grants to foster care (important to the growing number of HIV/AIDS orphans) and the disabled. The government's expenditure on HIV and AIDS has increased from R30 million in 1994 to about R4.6 billion in 2008. The very poor are steadily improving their lives through increased social assistance grants. The number of people benefiting has increased from 2.6 million to more than 10 million since 1994. The government continues to commission research to better understand the dimensions of poverty and the poverty gap, and to establish a poverty line so as to be able to monitor success.

18. Major Issues/Problems Identified: There are serious skills shortages throughout the economy. An area of particular concern for economists and the government is the shortage of skilled professionals such as doctors, nurses, math and science teachers, social workers, engineers, artisans, and project managers. Critics increasingly focus on problems with the education system and inadequacies in vocational training programs for not producing the skills that the country needs. The quality of South African schools remains uneven and education, though compulsory, is not free. The government has moved to fully subsidize schools in the poorest areas and all schools are officially required to inform parents that they may apply for fee exemptions. Nevertheless, school fees and associated costs for uniforms, books and stationery have an adverse impact on school attendance. The capacity of local government to administer services (administrative and physical infrastructure services), public-private partnerships, and welfare payments is limited.

Workers' Rights/Child Labor/Human Rights

19. Major Strengths Identified: The law recognizes workers' rights and provides for freedom of association, the freedom to organize and bargain collectively and the right to strike. Qto organize and bargain collectively and the right to strike. The law prohibits forced or compulsory labor, including forced child labor and the commercial sexual exploitation of children. The government is ahead of its target in implementing child benefits grants, now available to children 14 and under. ILO Conventions 182 on the worst forms of child labor and 138 on the minimum age have been ratified. The Children's Act prohibits trafficking of children and the Child Protection Unit raises awareness of child trafficking and conducts investigations. On May 13, 2008, the South African magistrates' courts charged a Mozambican woman with child trafficking. This was the first child trafficking case in South Africa. The law provides for freedom of speech and of the press, and the government generally respected these rights. The law provides for freedom of religion and the government generally respected this right.

110. Major Issues/Problems Identified: Since 2006, strikes have become more violent. A strike by private security guards against their employers resulted in over 50 deaths. Police and strikers in other sectors clashed during a number of legal marches. Food price inflation caused the number of strikes in 2007 to reach a new record, with 11.5 million workdays being lost to strike activity, according to data

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published by the South African Reserve Bank. The trend has continued in 2008. In May 2008, the South African Municipal Workers Union (SAMWU) led a three-week strike in Heidelberg in which a teenager and a municipal worker were killed as a result of a disagreement between government contract workers and SAMWU members. Hundreds have died in the workplace due to unsafe working conditions. Health and safety regulations were often not observed when chemicals were used in agricultural work, and deaths in mining increased by 10%

between 2006 and 2007. Although labor laws protected farm workers, some farm workers' unions encountered difficulties trying to organize workers. Farm workers or farm residents who attempted to organize were harassed, dismissed and/or evicted. Child labor remains a problem in the information and agricultural sectors, partly fueled by the impact of HIV/AIDS in creating poverty. Child sexual exploitation continued to be an issue. Most prisons did not meet international standards, and prison conditions did not always meet the country's minimum legal requirements. Violence against women is pervasive. Societal attitudes and a lack of infrastructure, resources, and training for law enforcement officials hampered the implementation of domestic violence legislation. Violence against children, including domestic violence and child rape remains widespread. Despite increased attention to the problem, a lack of coordinated and comprehensive strategies to deal with violent crime impeded the delivery of needed services to young victims. Police forcibly dispersed several demonstrations during 2007 which resulted in injuries. Some of the demonstrations had turned destructive prior to the police taking action to break them up.

International Terrorism/U.S. National Security

¶11. Major Strengths Identified: South Africa is a party to 11 of the 12 UN counter-terrorism conventions and protocols and has ratified nine of the 11 as well as the African Union Convention of the Prevention and Combating of Terrorism. In May 2005, South Africa enacted comprehensive anti-terrorism legislation entitled, the Protection of Constitutional Democracy Against Terrorist and Related Activities Act, which required citizens and financial institutions to report suspicious activity to law enforcement and allowed terrorist assets to be seized. South Africa remains a member of the Financial Action Task Force, an intergovernmental organization that combats money laundering and terrorist financing.

¶12. Major Issues/Problems Identified: South Africa must still become a party to and ratify three of the UN counter-terrorism conventions, including: Safety of Maritime Navigation, Safety of Fixed Platforms on the Continental Shelf and Protection of Nuclear Material. South Africa needs to take stronger steps to secure its identity documents and passports.

LA LIME